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SUBJECT: TAJIKISTAN: WHY MOUNTING CORRUPTION MATTERS

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11. (U) SUMMARY: Tajikistan's mounting corruption exacerbates growing income inequalities and degrades the relatively high human capital left from Soviet times. Pervasive corruption limits local and international investment, distorts donor and government development strategies, and undermines economic development. Tajikistan could drop to a lower growth path, despite the country's economic potential, if this problem is not addressed soon. END SUMMARY.

PERVASIVE CORRUPTION COSTS INCREASING

12. (SBU) Corruption levels in Tajikistan continue to climb with economic growth. Although there are no official corruption statistics, anecdotal evidence and an upcoming corruption report by a government think tank indicate the magnitude of the problem (REFTELS A and B) is growing. The current bribe, for example, for getting a railcar of goods through the standards process has risen from \$200 to \$400. Getting a loved one out of prison can run upwards of \$1,000. Moreover, paying to get a job and even paying for University grades and degrees are becoming engrained in society, and there is constant pressure to make payments years after getting domestic employment. The typical scenario involves an uncle getting his nephew a state job; the nephew not only owes his uncle, but then is responsible for permanently providing perks to the rest of the uncle's family, his wife, his wife's family, and others.

CORRUPTION DOESN'T TRICKLE DOWN

13. (U) Corruption exacerbates Tajikistan's growing income

stratification because the new wealth does not trickle down to the poor. This hinders development of a middle class, which is critical for fair and sustainable growth. The World Bank notes that while the aggregate poverty level declined in Tajikistan by 18 percentage points between 1999 and 2003, the Gini index that measures income inequalities has widened from .33 in 1999 to .36 in 2003. This is most notable in urban areas and Khatlon. In a country with a GDP per capita of \$310, this is extremely worrisome. The vast majority of the country's remittances -- estimated at 50 percent of GDP from the 30 percent of its males in migrant labor -- go towards poverty alleviation, and not investment.

¶4. (SBU) The World Bank reports that the country's \$2 billion GDP is insufficient to sustain the capital stock inherited from Soviet times. Even though most children still go to school, real education levels have plummeted, especially for girls. In an April 6 conversation with an international financial official married to a Tajik woman, he told PolOff he was surprised to learn when he returned to Dushanbe that many subjects -- such as math -- are simply dropped from the curriculum when there are no teachers. In a visit to a village an hour out of the northern city of Isfara, PolOff met the local teacher responsible for teaching all students in the village school; it was clear the woman had just graduated from the village school herself.

DISCOURAGES LOCAL AND INTERNATIONAL INVESTMENT

¶5. (SBU) Tajikistan's increasing corruption limits local and international investment. This fundamentally deters small and medium-sized enterprise growth, which is an integral part of sustainable economic development. Local businesses also do not expand because of the unofficial costs of doing business and because bribe costs keep escalating (REFTEL C). International investments are facing similar predicaments (REFTEL D). One international financial official believes the lack of local investment opportunities accounts for Dushanbe's and Kulob's

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residential building boom. A number of Tajiks who have between \$50,000 and \$500,000 see no place to invest it, so they put the money in the one place where supposedly it cannot be taken away from them: personal homes. This has resulted in a non-productive housing bubble in which new housing prices have no realistic correlation with income levels. An eye-popping number of these new homes are veritable McMansions. [COMMENT: Some new homes are much more than McMansions. The Embassy Housing Board was recently shown a palatial new compound in downtown Dushanbe. The owner pitched it as "perfect for the U.S. Ambassador." The price -- \$30,000 per month. The owner -- the Minister of Emergency Situations. END COMMENT]

SKEWS DEVELOPMENT STRATEGIES

¶6. (SBU) Mounting corruption distorts economic and social development strategies. Accountability is a vital component of designing effective programs to encourage equitable growth, but the hidden nature of corruption complicates formulating effective strategies. This impacts not only donor programs, but also President Rahmonov's policies and may account for his push for big infrastructure projects (easier to control the money) rather than truly promoting small and medium-sized enterprise growth. For example, if it is common to buy grades or educational degrees, then employers have little incentive to begin high-technology businesses and hire skilled local employees. But, building large infrastructure construction brings in foreign expertise and large (but temporary) cash flows to the economy.

¶7. (SBU) COMMENT: Sooner or later there will be a public backlash against corruption. Tajikistan is approaching a crucial crossroads, with a relatively high level of human capital and infrastructure from Soviet times that is rapidly deteriorating. Mounting pervasive corruption threatens to permanently undermine economic development and place the country on a lower growth path, despite Tajikistan's economic potential.

Tajik leadership seems to recognize this danger, but has not found a good strategy to deal with it. END COMMENT.

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HOAGLAND